

HOW MUCH CREDIT CAN YOU AFFORD?

FACT SHEET

Deciding how much credit you can afford is a personal financial decision. People have different wants, needs, goals and incomes, so they have different opinions on how to spend their incomes. Credit can be a valuable tool that offers many advantages, but there is a cost for using credit and too much credit can cause serious financial difficulties.

Deciding how much credit you can afford should be based on objective information from your income and expense records. With this information you can develop a spending plan that includes a list of your needs, wants and goals to direct your spending and saving. Without a plan for spending and saving it is very easy to overspend, especially with a credit card.

Guidelines For Setting Credit Limits

Answering the following questions can help you decide if you should use credit and how much credit is right for you and your family:

- **Should you use credit?** Most consumers use credit to purchase consumer goods such as cars and major appliances because they have the use of consumer goods while they pay for them. The following questions can help you decide if you want to use credit or cash:
 - How long will I have to save to pay cash?
 - How long can I wait to have the product?
 - Will the price be higher or lower in the future?
 - Will the convenience or satisfaction I gain from the product be worth the interest costs?
 - Will the monthly payment fit into my spending plan?
 - Will the product have value after I have finished paying for it?
- **Do you limit credit use to amounts that can be repaid from current and future income?** A spending plan is a way to control spending and saving so that you can meet your financial goals. It will help you analyze your income in relationship to your expenses. Then you can determine how much money you have available for credit use.
- **What percentage of your current after-tax income is already committed to credit debt?** List all credit commitments, such as automobile or consumer loans and credit cards. If you plan the use of credit, it can be a useful money management tool.
- **Have you established a debt limit?** It is important that you establish a debt limit based on your financial situation because many lenders are willing to lend more credit than you can afford. Use the debt limit to

control your credit use. Generally, financial planners suggest that from 10% to 20% of your disposable income is a realistic credit debt, excluding a mortgage.

How Much?

To determine how much credit you can afford, complete the following?

Monthly after-tax income	\$ _____
10% of after-tax income (pay X .1)	\$ _____
20% of after-tax income (pay X .2)	\$ _____
Monthly credit payments owed	\$ _____
(not including mortgage)	

- If your credit payments are less than or equal to 10% of your after-tax income you are controlling your credit use.
- If your credit payments are between 10% to 20%, you need to carefully evaluate any additional credit.
- If your credit payments are more than 20%, you should not take on additional credit.

These figures are general guidelines. Even though no two people spend their incomes the same way, most have some form of debt payments. In order to determine a realistic debt limit figure, consider the amount of current debt you have in comparison to your after-tax income.